COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

At Richmond, MARCH 20, 1998

COMMONWEALTH OF VIRGINIA

At the relation of the

STATE CORPORATION COMMISSION Case No. PUE970695

Ex Parte, In re: Promulgation of Guidelines for Special Rates, Contracts or Incentives pursuant to Virginia Code § 56-235.2 D

FINAL ORDER

Section 56-235.2 of the Code of Virginia was amended by the 1996 General Assembly to permit utilities to request special rates, contracts, or incentives for particular customers or classes of customers. Section 56-235.2 D, as amended, includes a subsection that requires the Commission to issue guidelines for special rates, contracts or incentives "that will ensure that other customers are not caused to bear increased rates as a result of such special rates." § 56-235.2 D of the Code of Virginia.

By Order dated September 16, 1997, the Commission provided notice, scheduled a hearing, and invited interested parties to file written comments and to propose additions, modifications or deletions to the Guidelines recommended by Commission Staff.[1]

On January 20, 1998, Chief Hearing Examiner Deborah V. Ellenberg issued her Report. She incorporated the suggestion of Washington Gas Light Company and Shenandoah Gas Company that the heading of the Guidelines be changed from "Electric Service" to "Utility Service" to clarify that the Guidelines will apply to all utilities. The Hearing Examiner found that, on the whole, the participants raised three common concerns: (1) a need for greater guidance as to what constitutes compliance with the statutory standards; (2) a desire to establish time parameters for Commission review in order to expedite processing of applications under this provision; and (3) the need to provide for confidentiality of the provisions of contracts filed pursuant to § 56-235.2.

With respect to the request for greater guidance, the Hearing Examiner noted that the statute already establishes broad standards, requiring that the Commission ensure that a special rate, contract or incentive "(i) protects the public interest, (ii) will not unreasonably prejudice or disadvantage any customer or class of customers, and (iii) will not jeopardize the continuation of reliable electric service." § 56-235.2 C of the Code of Virginia. The Hearing Examiner rejected the suggestion of certain of the participants that more specific criteria for approval of a special rate be developed. She shares Staff's concern that more experience should be gained with processing such applications before establishing more specific criteria. The Hearing Examiner found that the determination of whether a particular special rate satisfies the statutory

[1] The draft Guidelines were proposed by Staff and were included as an attachment to the September 16 Order. On November 26, 1997, Staff filed proposed revisions to the draft Guidelines that were based on its review of the comments filed by interested persons.

requirements of § 56-235.2 should be made on a case-by-case basis since the diversity of innovative proposals is thus far unknown.

One of the issues raised by participants in their initial comments was how a special rate, contract or incentive should be analyzed to determine its effect on the rates of other customers. That is, should the revenue derived from the special rate be compared with a presumptive absence of revenue, or should the revenue from the special rate be compared with revenue that would derive from existing tariffs. The Hearing Examiner agreed with the comments of certain participants that the standard for analyzing whether a special rate would cause other customers to bear increased rates should start with a determination of whether the revenues from the special rate would exceed the utility's variable costs of providing the service, noting that revenues in excess of variable costs would contribute to the recovery of fixed costs. She found, however, that in some cases, a complete analysis would also require a comparison of the revenues the utility would have generated if the customer had continued to take service under the existing tariff. The Hearing Examiner stated that the full analysis of any rate program should occur in a rate case and should take into consideration the particular circumstances regarding the loss of load or the attraction of new load. She also stated that all participants recognized that the rate analysis of a special rate should, and will, be part of a future rate case.

Based on her findings, the Hearing Examiner concluded that the draft Guidelines should not be changed with respect to the criteria for review of special rates. She did recommend, however, that a preamble should be added to the guidelines to define the general purpose of special rates and suggested the following language:

> These guidelines are applicable to special rates, contracts or incentives intended to prevent loss of existing load and/or to attract new load for the purpose of keeping rates to other customers lower

> than they would otherwise be given the probability of loss of such existing load or the failure to attract new load.[2]

The second primary concern addressed by the Hearing Examiner is whether the Commission should establish time limits for acting upon applications under § 56-235.2 in order to expedite the review of these applications. Neither Staff nor the Hearing Examiner supported the suggestion of certain of the parties that the Commission impose a timeframe within which it must act upon the application or have the application be deemed approved as filed by operation of law. While the Hearing Examiner recognized the need for prompt action on § 56-235.2 applications, she noted that these applications will vary widely in terms of the time required for adequate review and found that "[i]t would be unwise to establish specific time parameters for review without a better understanding of the scope and nature of the applications." Id. at 9. The Hearing Examiner observed that the statute requires that the Commission find that specific standards have been satisfied as a prerequisite of its approval and, therefore, the Commission cannot establish what would be, in essence, a default provision. In addition, she noted that the statute requires notice and hearing for applications under § 56-235.2; therefore, the Commission is not permitted to approve these applications, even noncontroversial ones, without a hearing.

With respect to the treatment of sensitive or proprietary material, the Hearing Examiner stated that clearly the burden of showing good cause to protect certain information from open disclosure falls on the party seeking such protection. She found that the language suggested by Appalachian Power Company, doing business in Virginia as AEP-Virginia ("AEP-Virginia"), would not shift the burden but would expedite the approval process by specifying measures for the preliminary treatment of information that may be sensitive or proprietary.[3] The Hearing

[2] Hearing Examiner's Report at 8.
[3] See id. at 6.

Examiner recommended that AEP-Virginia's language be adopted, with minor modifications.[4] She further recommended that, when a dispute arises, the burden to show that the information is material and necessary should shift to the party seeking the information after the party seeking to maintain protection shows that disclosure would be harmful.[5]

The Hearing Examiner also rejected the suggestion that the Commission should establish a customer usage threshold that would trigger the analysis of the rate impact of a special rate, contract or incentive. She found that no evidence was presented to support the assertion that a special rate offered to a customer below a certain size would have no adverse impact on the other customers, a finding that is required by the statute, and concluded that a threshold for exemption applicable to all utilities should not be established. The Hearing Examiner proposed Guideline No. 7 which allows an exemption from the requirements of Guideline Nos. 5 and 6 if the utility can provide an alternative analysis to support a finding that its other customers would not be adversely affected. The Hearing Examiner found that, while limits will vary from utility to utility, such a limit should not exceed 5 MW and each utility seeking a threshold exemption should justify the size limit appropriate for its system.[6]

Comments on the Hearing Examiner's Report were filed by AEP-Virginia, the Virginia, Maryland and Delaware Association of Electric Cooperatives ("Association"), and Virginia Electric and Power Company ("Virginia Power"). These three parties generally supported the Guidelines as modified by the Hearing Examiner, but nevertheless proposed certain changes.

Specifically, AEP-Virginia urges the Commission not to adopt the Hearing Examiner's proposed preamble, asserting that the preamble "would cause uncertainty about the scope of the

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[4] See Guideline No. 2.
[5] Hearing Examiner's Report at 8-9.
[6] Id. at 10.

Guidelines and detract from their effectiveness." AEP-Virginia Comments at 2. AEP-Virginia is concerned that the preamble's language could be interpreted to apply only to special rates that would prevent the loss of existing load or attract new load, but asserts that there could be other categories of special rate, contracts or incentives. AEP-Virginia contends that this language could be construed to imply that other possible categories of special rates may be impermissible or, if permissible, need not satisfy the Guideline's criteria. Moreover, AEP-Virginia asserts, the preamble is unnecessary.

In addition, AEP-Virginia continues to believe that language providing for the expedited treatment of applications for special rates should be added to the Guidelines. It states that the General Assembly could not have intended for lengthy notice and hearing requirements since uncertainty about the length of the approval process could negatively impact the parties' ability to negotiate special rates. AEP-Virginia states that there are alternative ways of providing for notice and hearing. It urges the Commission to establish a standard, expedited procedure for notice and hearing, noting that the Commission could provide for an exception for more extended procedures in more complex cases.

Finally, AEP-Virginia is concerned that Guideline No. 5, suggested by the Hearing Examiner, appears to require applicants to compare rates of return on equity calculated by customer class. It contends that such a requirement would require a substantial effort, similar to the effort required by a cost-of-service study, would slow down the approval process and may not be necessary in the context of special rates, contracts or incentives. It suggests that the phrase "return on equity" in Guideline No. 5 be replaced by the phrase "increased or decreased contribution to fixed cost" and that the remainder of the sentence after the word "applicable" be

deleted.[7] AEP-Virginia also suggests that Guideline No. 7, which provides for an exemption from compliance with Guideline Nos. 5 and 6 for customers with loads no greater than 5 MW, be modified in a way that would avoid the creation of unnecessary procedural steps that could delay the review process. Specifically, AEP-Virginia recommends that the first sentence of Guideline No. 7 be changed to read: "Requests for special rates, contracts or incentives for customers with total load no greater than 5 MW need not comply with Guidelines 5 and 6." Id. at 5.

The Association supports the Hearing Examiner's recommendations and requests only that the Commission reconsider the issue of whether a timeframe for the processing of § 56-235.2 applications should be established. The Association believes that establishing time parameters, or even the provision of a general statement of the Commission's intent to act on applications within a certain time, would be beneficial given the time sensitivity of special rate proceedings.

Virginia Power generally endorses the Hearing Examiner's modifications to the Guidelines as reasonable, appropriate and supported by the record; however, it requests three additional clarifications or changes. First, it requests that the Commission clarify that the words "new load" in the proposed preamble refer to new customers' loads and the new load of an existing customer that has expanded as a result of the availability of a special rate.

Second, Virginia Power continues strongly to recommend that time parameters for acting on the applications be established. It states that while it agrees with the Hearing Examiner that some applications will be more complex than others and that each application should be addressed

[7] Thus, AEP-Virginia proposes to change the sentence that now reads: "Describe in detail the estimated effect that service provided under the proposed special rate, contract, or incentive will have on total company revenues, total company expenses, and on the return on equity or margins, if applicable, for the customer class in which the participating customer resides." to read: "Describe in detail the estimated effect that service provided under the proposed special rate, contract, or incentive will have on total company revenues, total company expenses, and on the increased or decreased contribution to fixed cost or margins, if applicable."

on its merits, it believes that these considerations should not preclude the imposition of a deadline for Commission action. Virginia Power suggests a ninety day time limit for evaluation, notice and final action on § 56-235.2 applications and that, if the Commission does not act within ninety days, the application be deemed completed and approved as filed.

Third, Virginia Power contends that the Hearing Examiner's Report failed to address correctly the requirement that an applicant provide information on the estimated effect that service provided under a proposed special rate would have on the applicant and its customers. The Company asserts that in situations involving new, previously unserved load, the load of an expanding customer or the prevention of loss of an existing customer, the comparison should be the increased margins derived from providing service to the load under the special rate, as opposed to not serving the load at all. Virginia Power believes that this approach will recognize that, without the special rate, load could be lost and "the Commonwealth will lose the opportunity for economic growth." Virginia Power Comments at 3. Virginia Power believes that the Guidelines should require an applicant to provide information that will enable Staff to determine that the proposed rate is designed to cover incremental costs, plus a margin as a contribution to the recovery of fixed costs. The Company asserts that this approach would ensure that special rates do not unreasonably prejudice or disadvantage any customer or class of customers and that other customers are not caused to bear increased rates as a result of the special rate.

NOW, upon consideration of the proposed Guidelines, the record herein, the Hearing Examiner's Report, and the comments thereto, the Commission is of the opinion and finds that the recommendations of the Hearing Examiner are supported by the record and should be adopted, with the modifications discussed below.

As an initial matter, we will clarify the scope of the Guidelines. Section 56-235.2 is confusing. Subsection A clearly applies to all utilities and was amended in 1996 to provide for special rates, contracts or incentives. Subsection B allows alternative regulatory plans for electric utilities only. Subsection C applies to both A and B, and subsection C (iii) refers to electric service. Subsection D provides for the Commission to promulgate guidelines for the special rates allowed in Subsection A. Although notice of the proposed Guidelines was provided to all utilities and to the general public, only electric and gas utilities have participated in this proceeding. As mentioned, the Hearing Examiner adopted the suggestion of Washington Gas Light Company and Shenandoah Gas Company that the heading of the Guidelines be changed from "Electric Service" to "Utility Service" to clarify that the Guidelines would apply to all utilities. Given that this proceeding has addressed the proposed Guidelines as they would apply to gas and electric utilities only, we conclude that the Guidelines approved in this docket will be applicable to only gas and electric utilities.[8]

The proposed Guidelines, as modified by the Hearing Examiner, appear to implement effectively the General Assembly's directive that the Commission issue guidelines that "will ensure that other customers are not caused to bear increased rates as a result of such special rates," as required by § 56-235.2 D of the Code of Virginia. Moreover, the Guidelines incorporate the criteria set forth in § 56-235.2 C of the Code of Virginia. We agree with the Hearing Examiner that it is prudent to review § 56-235.2 A applications on a case-by-case basis and gain experience before identifying more specific criteria. We believe that the Guidelines will provide sufficient direction to applicants for an acceptable application under § 56-235.2 A while, at the same time,

[8] The Commission will adopt guidelines for utilities other than gas and electric utilities as needed.

the standards are not so particularized that they will discourage or preclude innovative special offerings.

With respect to the standard that requires a finding that other customers will not bear increased rates as a result of a special offering, AEP-Virginia and Virginia Power continue to assert that the Commission should not require applicants for special rates to compare rates of return because that requirement would slow down the approval process. They contend that it should be sufficient to show that the special rates would result in any contribution to the system.

We disagree. The Hearing Examiner found that the determination of whether other customers will bear increased rates as a result of a special offering should begin with a determination of whether the revenues from the special rate will exceed the utility's variable costs of providing the service but also include the impact of the special rate on total company revenues and expenses. The Hearing Examiner recommended a wording change to Guideline No. 5 to clarify that the Commission may not always require an examination of the rate of return for the customer class in which the participating customer resides. We agree with the Hearing Examiner that we cannot at this time know all of the possible situations in which special rates may be proposed or the diversity of special offerings that may be devised, and we believe that the public interest is best served by providing the Commission the flexibility to evaluate a proposal using whatever kind of analysis that it determines to be appropriate in a particular case. Therefore, we will adopt her proposed language, slightly modified, to require an applicant to "[d]escribe in detail the estimated effect that service provided under the proposed special rate, contract, or incentive will have on total company revenues, total company expenses, and, *if appropriate*, on the return

on *rate base* for the customer class in which the participating customer resides."[9] Our modification to the Hearing Examiner's recommended language should clarify that the Commission will not limit itself to a single means of evaluation but will use whatever analysis is appropriate for the particular proposal.[10]

We also wish to clarify that the statutory standards impose upon us the responsibility to analyze the rate impact of a proposed special rate, contract or incentive on individual customers or on a small group of customers, as well as on the remaining customers as a whole. This requirement is found in § 56-235.2 C (ii) which provides that the Commission must ensure that any special rate, contract or incentive "will not unreasonably prejudice or disadvantage <u>any customer</u> or class of customers." § 56-235.2 C of the Code of Virginia (emphasis added).

Although the Hearing Examiner did not recommend changing the Guidelines to identify more specific criteria, she did recommend an introductory statement to help define the general purpose of special rates, contracts or incentives. We will not add the proposed preamble. First, we do not believe that it is necessary. Second, we are concerned that the language contained therein may be construed as implicitly assuring utilities that any revenues that may be "lost" as the result of a customer no longer taking power from the utility or purchasing electricity pursuant to a special rate under § 56-235.2 A will be automatically recovered from the remaining customers. We emphasize that we do not make any such finding in this order. Utilities historically have borne

[9] We think "if appropriate" is more descriptive than "if applicable." We have deleted the reference to margins and provided for rate of return on rate base, rather than equity, because historically margins and rate of return on equity have not been calculated by customer class and we believe that rate of return on rate base will provide sufficient information.

[10] Similarly, Virginia Power suggests that the Guidelines should require an applicant to provide information that will enable Staff to determine that the proposed rate is designed to cover incremental costs, plus a margin as a contribution to the recovery of fixed costs. We find that the requirement of such a showing already is implicit in Guideline No. 5 since it requires applicants to detail the estimated effect that the special rate would have on total company revenues and total company expenses.

the risk of losing customers as a result of, for example, a customer's decision to self generate or to relocate to a different state. The Commission does not guarantee that a utility is entitled to recover from the remaining ratepayers any revenue it would have received under a rate or tariff approved by the Commission if one or more customers leave the system.[11]

With respect to the suggestion that time limits be imposed, we will adopt the Hearing Examiner's recommendation not to establish a timeframe within which § 56-235.2 applications must be acted upon or be deemed approved as filed by operation of law. We agree with the Hearing Examiner that to impose a time limit could conflict with the statutory requirements. For example, such a requirement would, in effect, create a default provision and the statute clearly requires that certain criteria must be met prior to Commission approval. We appreciate the parties' concern that applications under § 56-235.2 A be processed promptly given their time-sensitive nature, and we assure the participants that the Commission will endeavor to expedite its review of applications under Va. Code § 56-235.2 A to the extent possible.

With respect to the confidentiality of sensitive or proprietary material, we find that the Hearing Examiner's recommended treatment is reasonable and supported by the record.

Certain additional issues need to be addressed. AEP-Virginia expresses concern that the preamble will be construed to limit the kinds of applications that may be filed pursuant to § 56-235.2 or to imply that applications other than the kind that would prevent the loss of existing load or attract new load need not meet the criteria of § 56-235.2. In response to this concern, we now clarify that the Guidelines are applicable to special rates, contracts or incentives that may include,

[11] See, e.g., Application of Virginia Electric and Power Company, Case No. PUE940080, 1995 SCC Ann. Rept. 334, 335 (Approving an experimental program for industrial customers that could result in a loss of revenue of more than six million dollars a year and clarifying that the Commission would make no finding at that time whether any potential losses could be recovered from ratepayers).

but are not limited to, those that are intended to prevent the loss of existing load and/or are intended to keep or attract new load for the purpose of producing rates to other customers lower than they would otherwise be, given the probability of loss of such existing load or the failure to attract new load.

With respect to the minimum usage threshold for analysis, we will not adopt the recommendation that loads of 5 MW or less be automatically exempted from the Guidelines' required rate impact analysis. As discussed, the Hearing Examiner found that there is no evidence in the record to support such an exemption. Moreover, giving a special rate to a small customer or small portion of a utility's load may not have a significant impact on the utility's remaining customers as a whole, but could unreasonably prejudice or disadvantage an individual customer or a small group of customers which, as discussed above, is prohibited by § 56-235.2 C. Thus, the Commission will not establish an automatic exemption from the requirement of analyzing the rate impact of a proposed special rate for a load of any size since the statute requires that we evaluate the proposal's impact on individual customers as well as on the customer classes.

Under the Hearing Examiner's approach, an applicant may apply for an exemption from the requirements of Guideline Nos. 5 and 6 for loads up to 5 MW, and the Commission may grant the exemption if it finds that the proposal will not adversely affect other customers. We will modify Guideline No. 7 to make clear that the showing must also address individual customers and customer classes. Further, we clarify that the 5 MW maximum level pertains to a customer with a load of 5 MW or less or could apply to a group of customers whose aggregate load is not

greater than 5 MW; thus, electric utilities are not prohibited from requesting more than one exemption.[12]

Accordingly, IT IS ORDERED THAT:

(1) The findings and recommendations of the January 20, 1998 Hearing Examiner's Report are adopted, with the modifications discussed herein and the Guidelines, in the final form found in the attachment to this Order, are approved and will become effective as of the date of the issuance of this Order.

(2) This matter shall be dismissed and removed from the Commission's docket of active proceedings.

[12] Guideline No. 7 by its terms applies only to electric utilities; the gas utilities did not request such a provision.

CHAPTER 310
Guidelines for Filing an Application to Provide Electric and Gas Service under a Special Rate, Contract, or Incentive

20 VAC 5-310-10. Guidelines for special rates, contracts, or incentives.

Any application for approval of a special rate, contract, or incentive filed pursuant to § 56-235.2 of the Code of Virginia shall:

1. Explain in detail the intended purpose of the special rate, contract, or incentive and why current tariffs of the utility are insufficient. Explain how the proposed special rate, contract, or incentive (i) will protect the public interest, (ii) will not unreasonably prejudice or disadvantage any customer or class of customers, and (iii) will not jeopardize the continuation of reliable utility service.

2. Provide a copy of the proposed special rate, contract, or incentive. The applicant shall clearly mark any part of the application or supporting information which it deems should not be subject to public disclosure as "confidential information." Unredacted copies of documents containing information so marked shall be withheld from public disclosure by the Clerk of the Commission for Commission and Staff review unless disclosure is ordered by the Commission. Copies of documents redacted to exclude confidential information shall be filed and placed in the public file. By Commission order or agreement with the applicant, other participants may be provided unredacted copies of documents containing confidential information but shall not disclose confidential information to any person unless permitted to do so by the Commission order. The burden for proving the need to maintain confidential treatment will remain with the party seeking it. No Commission order shall be issued under this subdivision without notice to the applicant and the owner of such confidential information and an opportunity for them to address the Commission with respect to its confidentiality.

3. Describe the characteristics of the customers to whom the proposed special rate, contract, or incentive would apply and, if applicable, identify the tariff under which each such customer would otherwise have taken service. Such characteristics should include, but not be limited to, load factor, load diversity, energy use, and peak demand, and may include energy conservation alternatives.

4. Provide in detail the estimated direct costs incurred to implement the special rate, contract, or incentive.

5. Describe in detail the estimated effect that service provided under the proposed special rate, contract, or incentive will have on total company revenues, total company expenses, and, if appropriate, on the return on rate base for the customer class in which the participating customer resides.

6. Describe in detail the rate impact of the proposal on the company's other customers and explain how the company will ensure that other customers will be protected from bearing any increased rates as a result of the proposed special rate, contract, or incentive. Explain how the utility will allocate or use any resulting benefits.

7. Utilities may seek an exemption from the analysis required in subdivisions 5 and 6 for customers with total loads aggregating no more than 5 MW. Any such request shall provide an alternative analysis to support the findings required by § 56-235.2 C and D.